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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1942

No. 658

ANTOINETTE K. BROWN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1942

No. 658

ANTOINETTE K. BROWN,

vs. *Petitioner,*

COMMISSIONER OF INTERNAL REVENUE.

PETITION FOR REVIEW ON WRIT OF CERTIORARI OF THE DECISION OF THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

To the Honorable the Supreme Court of the United States:

Antoinette K. Brown, the petitioner, respectfully presents this petition for review on writ of certiorari of a decision of the United States Circuit Court of Appeals for the Third Circuit.

Opinions Below.

The first opinion of the Board of Tax Appeals is reported at 42 B. T. A. 693. The first opinion of the Circuit Court of Appeals is reported at 122 F. (2d) 800. The second opinion of the Board of Tax Appeals is reported

at 46 B. T. A. 782. The second opinion of the Circuit Court of Appeals is reported at — F. (2d) —.

Statement of the Matter Involved.

The petitioner in 1927 established an irrevocable trust, the income of which was payable outside the family group, $35.00 a month to a retired servant, and the balance to a friend. The Commissioner in 1939 (12 years later), for the first time asserted that the trust income was taxable to petitioner (under Sections 166 and 167 of the Revenue Act) and determined a deficiency of $11,133.06 in petitioner's income tax for 1935. A description of the trust agreement as found in the opinion of the Circuit Court of Appeals of November 20, 1942 (R. 48), is as follows:

> "* * * The purpose of the trust was not to effect a saving in income taxes. The term was for the life of the settlor. Upon termination of the trust the corpus was to go to her estate. The settlor retained the power to modify the trust: 1. She could increase the principal. 2. She could change both the beneficiaries and the proportion of the income payable to any beneficiary except that such changes could not be for the benefit or use of the settlor. 3. She could (and did) substitute trustees. 4. Similar powers of modification were retained as to the disposition of the corpus upon the settlor's death as were retained with respect to income during her lifetime."

Petitioner did not exercise any of her reserved rights until after 1935 when she made her husband, Paul G. Brown, Trustee, and at the death of the friend in 1937 she made him the beneficiary in her place and stead. The husband had income from other sources at least equal to petitioner's income (R. 22). The Commissioner has also asserted that the trust income is subject to gift taxes amounting to $14,000.00, exclusive of interest (R. 27).

The Board of Tax Appeals, in its first opinion (R. 6), held (1) that the Commissioner could not be sustained on the argument that the trust was revocable because it provided for no estate in remainder; (2) that Sections 166 and 167 of the Revenue Act of 1934 did not apply; and (3) as to Section 22(a) resorted by the Commissioner for the first time in his brief, that the petitioner had never had an opportunity to be heard on this point, and further (R. 8):

> "Here, however, the Commissioner has failed to make a case. He cites *Helvering* v. *Clifford,* 309 U. S. 331. The case is not in point * * *."

On review, the Circuit Court of Appeals unanimously agreed with the Board that the income of the trust was not taxable to petitioner under Sections 166 and 167 but divided on the question whether the income was taxable to petitioner under Section 22(a). The decision of the Board was reversed and the cause remanded to the Board "with direction to permit the parties to adduce additional evidence and to decided the issues presented by Section 22(a)" (R. 14).

After further hearing, at which petitioner offered the testimony of one witness (originally the facts had been stipulated), the Board decided that as the stipulation and the new evidence made no stronger case for the petitioner than did the stipulation alone, the law as established by the Circuit Court of Appeals must stand, and therefore the income of the trust is taxable to the petitioner under Section 22(a) of the Revenue Act of 1934 (R. 35).

On appeal from this decision, the Circuit Court of Appeals for the Third Circuit affirmed the decision of the Board (R. 50).

Jurisdictional Basis.

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended (Title 28) Code of

the Laws of the U. S., Section 347) to review the decision of the United States Circuit Court of Appeals for the Third Circuit entered on November 20, 1942.

The Questions Presented.

1. Is the question of ownership of trust income a question of fact which, if supported by substantial evidence, makes the decision of the Board of Tax Appeals binding upon the Circuit Court of Appeals?

2. Whether trust income permanently and irrevocably dedicated for the use and benefit of others than the settlor may be treated for tax purposes as belonging to the settlor because of unexercised reserved powers to change beneficiaries.

3. Did the Circuit Court of Appeals err in holding that under the guiding precedents, beginning with *Helvering* v. *Clifford,* 309 U. S. 331 (1940), and *Helvering* v. *Horst,* 311 U. S. 112 (1940), and ending with *Helvering* v. *Stuart,* 63 U. S. 140 (1942), the income of petitioner's 1927 trust was includable in her 1935 income under Section 22(a) of the Revenue Act of 1934?

Reasons Relied Upon for Allowance of the Writ.

I. The decision of the Circuit Court of Appeals for the Third Circuit is, on the first question as above presented, in direct conflict with decisions of the Circuit Courts of Appeals of the Sixth and Seventh Circuits. This conflict is set out and commented on in the opinion of the Circuit Court of Appeals as follows (R. 49):

> "This argument finds support in *Commissioner of Internal Revenue* v. *Armour,* 125 F. (2d) 467 (C. C. A. 7, 1942) and *Commissioner of Internal Revenue* v. *Goulder,* 123 F. (2d) 686 (C. C. A. 6, 1941). It stems

from certain language in the opinion of the Supreme Court in *Helvering* v. *Clifford* which was thoroughly examined and discussed by the Second Circuit in *Commissioner of Internal Revenue* v. *Berolzheimer,* 116 F. (2d) 628 (C. C. A. 2, 1940). We agree with that decision. * * *''

II. There are no decisions of the Supreme Court which have removed the uncertainty of the rule to be applied in this case and many other like cases now before the courts. As pointed out in *Cory* v. *Commissioner,* 126 F. (2d) 689 (C. C. A. 3):

> ''Hardly had the *Clifford* decision been promulgated when repercussions were heard. It has been said that few tax problems in recent years have caused as much litigation as this one decision.
>
> ''The principal difficulty lies in the fact the Supreme Court's decision merely roughed in the broad outline of taxability and left the completion of the picture to future decisions.''

III. In *Helvering* v. *Stuart, et al.,* 63 U. S. 140 (11/16/42), cited by the Circuit Court of Appeals in its opinion in the case at bar, the Supreme Court held that since under the Illinois Law the power given to two non adverse interest co-trustees (wife and brother) of the grantor to change the income beneficiaries could not be exercised by them for grantor's benefit (same in the instant case under the New York law), the income was not taxable to him. The court distinguished the *Stuart* case from the *Clifford* case by pointing out and emphasizing the distinction between the ''economic gain'' which the grantor may obtain through control of a trust and ''non-material satisfactions'' which he may derive from the exercise of a power to direct the distribution of income to others than himself and for which the court declares him non-taxable. And yet, in the case at bar, the trust income is taxed to petitioner because of

these "non-material satisfactions." Even in the later years not here at issue, when petitioner's husband was in receipt of part of the trust income, petitioner derived no "economic gain" thereby because, as established by the evidence, his taxable income was in excess of her income.

IV. This petitioner is entitled to certainty when arranging her affairs and it is inequitable to change the rules by "judicial legislation" when the rules followed for deflection of the income here at issue, not rendered nugatory by statute, have for some time been successfully used with the acquiescence of the Commissioner and without imposition of penalizing taxes.

V. Petitioner cannot achieve status quo by surrendering her power to reallocate the trust income because of the gift taxes now asserted against her. Yet in 1927, when the trust was created, and for many years thereafter, even the Commissioner did not contend that taxpayers in this class of cases were taxable on trust income under Section 22(a). In this very case the Commissioner relied solely upon Sections 166 and 167 of the Revenue Act of 1934 and it was not until after the case was heard in the Board that the Commissioner in his Brief raised this issue.

VI. The test of the *Clifford* case as to whether or not the petitioner was poorer after the creation of the trust, and the harshness of the rule now contended for by the Commissioner, are aptly, even though only theoretically, met and demonstrated if we take an illustration used in 51 Yale Law Journal, 213, 249 and apply it to the facts of this case.

Assume that petitioner, being of an adventurous turn of mind or urged into losing ventures by outside influences, had, as a result of the panic of 1929, lost everything she had, including her husband, and only the trust assets and trust

income remained. The consequent trust income would, in 1935, be taxable to the now penniless petitioner and in addition to income taxes she would owe each year a gift tax. No change in beneficiaries could divert trust income to the payment of these taxes because by the terms of the trust agreement the income cannot be "paid or applied to the use or benefit" of petitioner.

WHEREFORE, It is respectfully submitted that the Supreme Court should grant this petition for review on writ of certiorari of the decision of the Circuit Court of Appeals for the Third Circuit.

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In the Supreme Court of the United States

OCTOBER TERM, 1942

No. 658

ANTOINETTE K. BROWN, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The first opinion of the Board of Tax Appeals (R. 4–8) is reported at 42 B. T. A. 693. The first opinion of the Circuit Court of Appeals (R. 9–16) is reported at 122 F. (2d) 800. The second opinion of the Board of Tax Appeals (R. 32–35) is reported at 46 B. T. A. 782. The second opinion of the Circuit Court of Appeals (R. 47–50) is reported at 131 F. (2d) 640.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on November 20, 1942 (R. 50). The petition for a writ of certiorari was filed January

18, 1943. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Taxpayer conveyed securities to trustees to pay the income to named beneficiaries during her life and upon her death to pay the principal to her estate. She reserved the right to alter the distribution of the income among the beneficiaries and to change the beneficiaries at any time. She also reserved the right to remove the trustee at any time with or without cause, naming any new trustee she wished, and to designate at any time new remaindermen. Is the income of the trust taxable to the settlor?

STATUTE INVOLVED

Revenue Act of 1934, c. 277, 48 Stat. 680:

> SEC. 22. GROSS INCOME.
>
> (a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

STATEMENT

On January 1, 1927, the taxpayer, who was then a married woman more than sixty years old (R. 19) transferred certain securities to her brother in trust during her life, to pay thirty-five dollars a month of the income to a retired servant and the remainder to Josephine Ballard, a friend. Upon the taxpayer's death, the corpus was to be paid to her executors and administrators in their representative capacity. (R. 36, 38–46.) The trust was established for the purpose of providing support for Miss Ballard, who had come from a well-to-do family which had lost its money and who had been the taxpayer's lifelong friend (R. 20–21).

By the terms of the trust instrument, taxpayer reserved the right to increase the principal, to dispose of the income as she should see fit by altering its distribution among the beneficiaries or by designating new beneficiaries, except that taxpayer was not entitled to direct that the income be paid or applied to her use or benefit; to direct how the principal should be distributed upon her death; and to remove the trustee, with or without cause, and designate any new trustee, including herself. All these powers could be exercised at any time and from time to time. (R. 38–46.)

In 1936, after the close of the taxable year involved, taxpayer appointed her husband trustee in place of her brother, and in 1938, upon the death of Miss Ballard, named her husband as principal beneficiary of the income (R. 21–22).

The income of the trust for the taxable year 1935 was distributed in accordance with its terms but was not reported by taxpayer in her income tax return (R. 36–37). The Commissioner determined a deficiency, explaining that the income was taxable to the settlor under Sections 166 and 167 of the Revenue Act of 1934 (R. 6). Before the Board of Tax Appeals the Commissioner also contended that the income of the trust was taxable to the settlor under Section 22 (a) (R. 8). The Board of Tax Appeals held that the income was not taxable to the settlor (R. 4–8).

On appeal the Circuit Court of Appeals for the Third Circuit sustained the Board's decision as to Sections 166 and 167 but reversed as to Section 22 (a) and remanded the cause for additional evidence (R. 9–16). At the subsequent hearing before the Board of Tax Appeals, taxpayer's husband testified concerning the circumstances under which the trust was established and explained the relationship between the parties involved, as outlined above (R. 16–26). The Board, considering itself bound by the prior decision of the circuit court of appeals, held the income of the trust to be taxable to the settlor under Section 22 (a) (R. 32–35). On appeal the circuit court of appeals affirmed (R. 47–50).[1]

[1] Since the court below in its first opinion held Sections 166 and 167 inapplicable no question concerning them is raised by the petition. Should the petition be granted, however, we shall urge their applicability as an alternative ground supporting the decision upholding the tax.

ARGUMENT

The circuit court of appeals held that the taxpayer retained such a measure of control over the principal and income of the trust that, for reasons explained in *Helvering* v. *Clifford,* 309 U. S. 331, she was to be regarded as the owner of the property, and the income therefrom was to be attributed to her under Section 22 (a). See also, *Helvering* v. *Horst,* 311 U. S. 112; *Helvering* v. *Eubank,* 311 U. S. 122; *Harrison* v. *Schaffner,* 312 U. S. 579.

This decision is plainly correct. Taxpayer surrendered only the powers to dispose of the principal during her lifetime and to direct the payment of income to herself. In her situation, those incidents of ownership can hardly have been a matter of consequence; she was over sixty, married, and (apparently) financially secure. She retained all the incidents of ownership which were a matter of concern—the ultimate power of management and investment through her right to appoint new trustees at any time, the enjoyment of the income not only through the support of her lifelong friend but also through her right to name any new or different beneficiaries, including her husband, whenever she desired, and the substantial control of the principal through her power to control both the disposition of the income during her life and the distribution of the principal upon her death. Consequently, the instant case is well within *Helvering* v. *Clifford, supra,* and is quite unlike the

trust involved in *Helvering* v. *Stuart*, No. 48, this Term, decided November 16, 1942, by which no such measure of control was retained.

Moreover, there is no occasion for further review. Since the decision in the *Clifford* case, the principles invoked by the court below have been well settled; and the court's application of them to the facts of instant case is in accordance with the views of other circuit courts of appeals. See *Commissioner* v. *Buck*, 120 F. (2d) 775 (C. C. A. 2), approved in *Commissioner* v. *Bateman*, 127 F. (2d) 266 (C. A. A. 1); *Commissioner* v. *Wilson*, 125 F. (2d) 307 (C. C. A. 7); *Commissioner* v. *Betts*, 123 F. (2d) 534 (C. C. A. 7).

Although taxpayer does not contend that the ultimate conclusion that the income was taxable to her raises any substantial question or is in conflict with any other decision, she does assert that the reasoning of the court below conflicts with *Commissioner* v. *Goulder*, 123 F. (2d) 686 (C. C. A. 6), and *Commissioner* v. *Armour*, 125 F. (2d) 467 (C. C. A. 7) because the court below ruled that it was not bound by the ultimate conclusion of the Board of Tax Appeals. But any statement or inference in *Commissioner* v. *Goulder, supra*, that the ultimate issue is exclusively one of fact must be taken to have been repudiated by the same court in *United States* v. *Anderson*, decided December 2, 1942, 1942 Prentice-Hall, par. 63,095, where it was held that the ultimate conclusion of the Board in cases like

this is subject to review. Likewise, *Commissioner* v. *Armour, supra,* perhaps should be read in connection with *Commissioner* v. *Wilson,* 125 F. (2d) 307 (C. C. A. 7), which was decided by the same court three days before the *Armour* case, and which holds that the ultimate question is a mixed question of law and fact. In *Williamson* v. *Commissioner* (C. C. A. 7), decided December 29, 1942, 1943 Prentice-Hall, par. 62,382, however, the court reiterated the view that the ultimate question is one of fact. The composition of the court was different in each of these three cases and it is apparent that within the Seventh Circuit some confusion exists.

But, in any event, no conflict is raised by the instant case. Unlike the situation in the *Armour* and *Williamson* cases the instant case did not come before the court below on an ultimate finding of fact supported by substantial evidence. When the case was first before it, the evidence had not been directed to Section 22 (a) and the Board of Tax Appeals, treating the question as one of law to be decided upon the available precedents, ruled that the Commissioner had not made a case. This conclusion, moreover, whatever its character, was plainly erroneous upon the stipulated facts, and the circuit court of appeals was entitled to set it aside and to remand the cause with a correct statement of the applicable principles in order that the taxpayer might have an opportunity to introduce

evidence upon the applicability of Section 22 (a). The Board's decision upon the remand that the new evidence did not alter the case was unquestionably correct and the court below properly affirmed.[2]

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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FEBRUARY 1943.

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[2] In *Woolley* v. *Commissioner*, No. 743, October Term, 1941, the petition for certiorari urged the lower court erred in reversing (122 F. (2d) 167 (C. C. A. 2)) a decision of the Board of Tax Appeals holding the income of a trust not taxable to the grantor, because, under the *Clifford* case, the Board's ultimate finding, if supported by substantial evidence, was conclusive on appeal. The petition was denied, 314 U. S. 693.

U. S. GOVERNMENT PRINTING OFFICE: 1943